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IN THE

Supreme Court of the United States

OCTOBER TERM, 1934.

No. [redacted]6

JOHN A. NELSON COMPANY, *Petitioner*,

v.

COMMISSIONER OF INTERNAL REVENUE.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

J. S. SEIDMAN,
80 Broad Street,
New York City,
Counsel for Petitioner.

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JOHN A. NELSON COMPANY, *Petitioner*,

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COMMISSIONER OF INTERNAL REVENUE.

PETITION FOR WRIT OF CERTIORARI.

Petitioner, John A. Nelson Company, by J. S. Seidman, its counsel, prays that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Seventh Circuit entered in the above entitled case on February 23, 1935, affirming the decision of the Board of Tax Appeals in 28 B. T. A. 529.

Question Presented.

Where a taxpayer transfers substantially all of its assets to another corporation in exchange for all of the latter's preferred stock and a cash sum, and the taxpayer immediately distributes the preferred stock and cash so received to its own stockholders, and the taxpayer, though inactive, does not dissolve, does this constitute a reorganization within the meaning of Section 203(h) of the Revenue Act of 1926, the material portion of which for present purposes is as follows:

> "(1) The term 'reorganization' means (A) a merger or consolidation (including the acquisition by one corporation of * * * substantially all the properties of another corporation) * * *."

If, as petitioner contends, the answer is in the affirmative, no tax gain or loss results; if in the negative, tax gain or loss does enter. (See Appendix for more complete statement of applicable statutory provisions.)

Statement.

The issue here presented is not the creature of the parties, but of the Board of Tax Appeals (R. 39-40). *The parties stipulated that there was a reorganization* and their only contest was as to the tax effect of the reorganization (R. 13). A division of the Board promulgated an opinion (24 B. T. A. 1031) deciding the effect of the agreed reorganization (R. 26-39, especially 37-39). Thereafter, the Board, of its own motion, withdrew the opinion and ultimately promulgated another opinion (five members concurring in the result only, and one dissenting) declaring that there was no reorganization (R. 45-61, especially 58-60).

Petitioner was in the adding machine business (R. 12). On November 18, 1926, it entered into an agreement with Elliott-Fisher Company with respect to that business (R. 13). The agreement provided, among other things, for the organization by Elliott-Fisher Company of a new company with a capitalization of 12,500 shares of preferred stock and 30,000 shares of common stock (R. 14, 16). The terms of these stocks were set forth in detail (R. 14-16). Petitioner agreed to transfer all of its assets (except cash of $100,000, which constituted less than 3% of its assets), subject to all its liabilities, in exchange for the 12,500 shares of preferred stock and $2,000,000 in cash to be raised by the sale for that amount by the new company of 30,000 shares of common stock to Elliott-Fisher Company (R. 17, 18, 21-22). The new company was to have the right to use petitioner's name (then called the Sundstrand Corporation) and petitioner agreed, upon request, to change its own name for the purpose (R. 19). The date for the con-

summation of the transfer was fixed at December 31, 1926 (R. 20).

On November 18, 1926, a special meeting of petitioner's stockholders was held at which the foregoing agreement, described in the minutes as "providing for a reorganization" of the company and sale and transfer of its assets, was approved, and it was voted that upon the consummation of the transfer, the preferred stock and cash to be received from the new company be immediately distributed to petitioner's stockholders in the order of their preferential right (R. 23-24). It was also voted that "after the distribution of the proceeds in accordance with the reorganization plan", petitioner be dissolved (R. 24). It was voted, too, that in the meantime petitioner's name be changed to John A. Nelson Company so as to enable it to comply with the agreement (R. 24).

On December 31, 1926, the transfer and distribution were consummated, pursuant to the agreement of November 18, 1926 and the vote of petitioner's stockholders at the meeting of November 18, 1926 (R. 13).

Reasons for Granting the Writ.

1. Four decisions (including the one at bar) on the basic point have recently been handed down by the Circuit Courts of Appeals, and they are in sharp conflict with one another. Chronologically, the one at bar was first. The dissenting opinion of one of the others (holding for reorganization) and the prevailing opinion of a third (holding against reorganization) cite the instant case in support of the conclusions reached. In all likelihood, applications for writs will be applied for in all of these cases and will come up for consideration at the same time as this one.

Holding *for* reorganization:

C. C. A.—2: *John J. Watts* v. *Commissioner*, March 4, 1935, reversing 28 B. T. A. 1056; petition for rehearing denied March 27, 1935;

C. C. A.—8: *Minnesota Tea Company* v. *Commissioner,* March 25, 1935, reversing 28 B. T. A. 591 (dissent citing the present case).

Holding *against* reorganization:

C. C. A.—7: The present case, February 23, 1935, affirming 28 B. T. A. 529 and reversing 24 B. T. A. 1031;

C. C. A.—4: *The G. and K. Manufacturing Company* v. *Commissioner,* April 2, 1935, affirming unpublished B. T. A. opinion. (The present case cited in support of the Court's opinion.)

In each of these cases, the effect of absence of stock control over the transferee and of the continued existence of the transferor was the pivotal point. The Second and Eighth Circuits held these factors to be immaterial under the language of the statute, in determining whether a reorganization exists. The Fourth and Seventh Circuits held the other way.

2. Earlier decisions of the Circuit Courts likewise add to the conflict.

Holding *for* reorganization:

C. C. A.—6: *Harry C. Howard* v. *Commissioner,* 56 Fed. (2d) 781, affirming 20 B. T. A. 207. *Certiorari denied* 53 S. Ct. 19;

C. C. A.—4: *C. H. Mead Coal Co.* v. *Commissioner,* 72 Fed. (2d) 22, affirming on this issue 28 B. T. A. 599.

Holding *against* reorganization:

C. C. A.—10: *West Texas Refining and Development Company* v. *Commissioner,* 68 Fed. (2d) 77, affirming on this issue 25 B. T. A. 1254.

In these cases, the transferor had no stock control over the transferee, but did go out of existence. The Fourth and Sixth Circuits did not regard stock control as important. The Tenth Circuit held that the stockholders of the transferor must continue the same or practically the same percentage of stock interest in the transferee to constitute a reorganization.

3. The present decision is contrary to the principles laid down by the Supreme Court in *Pinellas Ice and Cold Storage Company* v. *Commissioner*, 287 U. S. 462. Reorganization was there said to exist if one corporation acquires substantially all of the assets of another, and the stockholders of the transferor have a continuing interest in the transferee.* Nothing at all was said about the necessity for control over the transferee or the dissolution of the transferor, or both. The imposition of these additional requirements by the Seventh and Fourth Circuits in effect confine reorganization to merger and consolidation in disregard of the statutory language in parentheses following the words "merger or consolidation", which is the very thing the Supreme Court decided against.

4. There is here involved an important question of income tax law, which now appears to be bathed in a hopeless sea of doubt. From 1921 until the Board's decision in *Minnesota Tea Company, supra*, in 1933, the regulations and rulings of the Treasury Department, and the decisions of the Board of Tax Appeals and the Courts, held *for* reorganization in the factual background presented by the instant case. These authorities were in turn basically

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* That preferred stock constitutes an interest in the corporation, see *Atlantic City Electric Co.* v. *Commissioner*, 288 U. S. 152, holding that "despite redeemability and the limitation of dividends, the owners of the preferred stock were not in the position of creditors, but were stockholders with a proprietary interest in the corporate undertaking * * *". Likewise, *Keen & Woolf Oil Company* v. *Commissioner*, 49 Fed. (2d) 45 (C. C. A. 5), where the Court declared that "'interest' refers to ownership, and may be retained either through preferred or common stock, and independently of voting power". To the same effect, see *I. Unterberg & Co.* v. *United States*, 64 Ct. Cls. 197.

grounded on the language and legislative history of the Acts. In reliance on these interpretations and the declared resulting absence of gain or loss, many corporations consummated transactions involving substantial amounts. The Board, beginning with the *Minnesota Tea Company* case, departed from these interpretations but with confusing inconsistency, even where, as in that case and in the present case, the Treasury Department agreed that there *was* a reorganization. This led to many and large additional assessments or assessment proposals, and to claims for refund (the latter, because of losses or increased depreciation deductions unallowable under the earlier interpretations).

As a result, there are many cases on the point now pending before the Board of Tax Appeals and the trial courts. In the Appellate Courts, *Helvering* v. *J. M. Harrison* is now before the Sixth Circuit on appeal from 30 B. T. A. 966, and in the Third Circuit, *Helvering* v. *Marjorie C. Langworthy* is pending on appeal from 30 B. T. A. 1217 (styled John S. Woodward before the Board). The reversal by the Eighth Circuit (and, in effect, the Second Circuit) of the Board's decision in *Minnesota Tea Company*, the case that started the discord, almost concurrent with decisions in the opposite direction by the Fourth and Seventh Circuits add to the troubled waters. It is altogether fitting, proper and necessary that the point involved be put finally at rest through the decision of the Supreme Court.

Wherefore, it is respectfully submitted that this petition should be granted.

J. S. SEIDMAN,
Counsel for Petitioner.

May, 1935.

APPENDIX—Applicable Statutes.

Section 203 of the Revenue Act of 1926:

"(b) (3) No gain or loss shall be recognized if a corporation a party to a reorganization exchanges property, in pursuance of the plan of reorganization, solely for stock or securities in another corporation a party to the reorganization."

"(e) If an exchange would be within the provisions of paragraph (3) of subdivision (b) if it were not for the fact that the property received in exchange consists not only of stock or securities permitted by such paragraph to be received without the recognition of gain, but also of other property or money, then——

(1) If the corporation receiving such other property or money distributes it in pursuance of the plan of reorganization, no gain to the corporation shall be recognized from the exchange * * *."

"(h) As used in this section and sections 201 and 204——

(1) The term 'reorganization' means (A) a merger or consolidation (including the acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation, or substantially all the properties of another corporation), or (B) a transfer by a corporation of all or a part of its assets to another corporation if immediately after the transfer the transferor or its stockholders or both are in control of the corporation to which the assets are transferred, or (C) a recapitalization or (D) a mere change in identity, form, or place of organization, however effected.

(2) The term 'a party to a reorganization' includes a corporation resulting from a reorganization and includes both corporations in the case of an acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation."